



## **BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI**

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### **POINT I**

**The Act does not confer power upon the Commission to force creditors of a solvent public utility holding corporation, which is easily able to pay its debts, to accept anything but cash in payment of such debts.**

(a)

There is no specific provision in the Act (as there is in Section 77 and old Section 77B and the present Chapter X of the Bankruptcy Act) purporting to empower the Commission to vary the terms of the contracts of creditors.

The District Court said (R. 132a) that if Congress had intended to confer such power, it would have said so. The Circuit Court held (R. 209) that if Congress had not intended to confer such power, it would have said so.

We suggest that the proper test should be the usual one of necessity. In fact, the Act specifically provides that the Commission must, in order to approve a plan, find the plan "necessary to effectuate the provisions of subsection (b)". Subsection (b) refers to the fundamental purposes of the Act, *viz.* the simplification of the capital structures of public utility systems, the equitable distribution of voting power and the integration of their operating properties.

In any event, when implied, not express, provisions in a statute are under consideration, only those things will be added by implication which are essential to a realization of the fundamental purposes of the statute and to achieve a reasonable, not an absurd, result.

The District Court sitting as a trial court found (R. 139a, 147a) that payment in stocks rather than cash was

"not necessary or appropriate to carry out the purposes of the Act" nor, on the basis of this record, was there any doubt but that the debentureholders could be paid in full and in cash and a plan could be consummated which would achieve all of the objectives of the Act.

When corporations which are insolvent or unable to pay their debts are involved, bankruptcy processes are available. Bankruptcy presupposes the necessity of varying the rights of creditors. Section 11(e) presupposes solvency and ability to pay debts. Its purposes are simplification and integration and not reorganization.

We submit that the Circuit Court erred when it attempted to write into the Act an arbitrary power, not granted by Congress, on the part of the Commission to vary the rights of creditors in the face of clear evidence, supported by the District Court's findings, that there was no necessity for such variance.

(b)

The action of the Commission here, as sustained by the Circuit Court, constitutes an appraisal method for the determination of creditors' rights and satisfaction of such rights by distribution of other securities. Such action disregards many rights and the right of a creditor to have his obligation measured by the exercise of his contract rights.\* Not only is there no authority in the Act for this, but the implication of such right would be to cast doubt upon the constitutionality of the entire Section 11(e). We submit that the appraisal method as applied here is a clear violation of the due process clause of the Fifth Amendment. Cf. *In re Preble Corporation*, 12 F. Supp. 1002 (S. D. Me., 1935, aff'd 84 F. 2nd 73); *In re Tennessee Publishing Co.*, 81 F. 2nd 463 (C. C. A. 6th, 1936) aff'd on other grounds (299 U. S. 18). These cases hold that the provisions of Section 77B providing for the

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\*NOTE: See the negative pledge covenants Appendix B

discharge of dissenting senior obligations by the appraisal method is unconstitutional.

## (c)

Nor is the case of *Otis & Co. v. Securities and Exchange Commission*, 323 U. S. 624 (1945) in point. This Court there held that, as a matter of contract law, a dissolution order under the Act did not effect a "liquidation" within the meaning of the charter so as to entitle preferred stockholders to par plus accrued dividends. We submit that, if the majority of this Court had agreed with the minority that the impact of the Act constituted a "liquidation"; the entire Court would have held, under the absolute priority rule (*Case v. Los Angeles Lumber Co.*, 308 U. S. 106, *Consolidated Rock Products Co. v. Dubois*, 312 U. S. 510), that the preferred stockholders were entitled to take all. We find nothing in the *Otis* case indicating that the rights of a creditor and a preferred stockholder are essentially the same. On this matter the District Court said (R. 133a):

"A holding that the creditor here is entitled to cash if his debt is to be paid is not in conflict with the doctrine announced in *Otis & Co. v. SEC*, U. S. , for the relation of a creditor to a solvent company is quite different from the relation that exists between the stockholders *inter sese*.

In a case of preferred stock vs. common stock, such as was involved in *Otis & Co. v. SEC*, preferred does not necessarily receive its contractual liquidating rights because where simplification by nominal (but not actual) liquidation is compelled under the Act, charter provisions do not apply. That being so, claims of preferred are not matured and are consequently not a debt. [Footnote 8 is here omitted] In the case of bondholders, it is elementary a debtor-creditor relationship exists from the time the bond is issued. The claim of a bondholder may not always be matured in the sense that he can demand payment, but his is always a matured obligation in the sense that debt exists *eo instanti* and from the time of its contractual conception."

## POINT II

Even if the Act be construed to confer power upon the Commission to vary the contracts of creditors, the present plan is not fair, equitable, necessary or appropriate.

(a)

The Act specifically requires findings that the Plan, to be enforceable, be fair, equitable, necessary and appropriate.

There is no substantial evidence in the record to justify the Commission's finding that the Plan is necessary. The District Court refused to find that the Plan was appropriate (R. 147a).

As we have seen the District Court has found and the record is clear that the debentureholders could be paid in cash, in accordance with their contract, without hardship or injury to anyone.

The words "fair and equitable" have a well defined meaning both in equity and bankruptcy reorganization law. They are words of art and connote, among other things, the strict priority doctrine. *Case v. Los Angeles Lumber Co.*, 308 U. S. 106.

Since the decision of *Otis & Co. v. Securities and Exchange Commission*, *supra*, there is no doubt that the term "fair and equitable" has the same meaning under the Act that it has been given in equity and bankruptcy reorganization law. This Court there said:

"Like the bankruptcy and reorganization statutes, the Public Utility Holding Company Act, in providing that plans for simplification be 'fair and equitable', incorporates the principle of full priority in the treatment to be accorded various classes of security interests."

Therefore, the fairness and equity of the Plan is to be tested by the standards heretofore established by this Court. Among such standards are those established in *Consolidated Rock Products Co. v. Du Bois*, 312 U. S. 510 (1941), that "full compensatory provision must be made for the entire bundle of rights which the creditor surrenders". Such standards also include the principle stated in *Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific Railroad*, 318 U. S. 523 (1943), that where junior interests participate in a plan, the Commission and the Court should determine *what* the senior security holders should receive "in addition to a face amount of inferior securities equal to the face amount of their old one, as equitable compensation, qualitative or quantitative, for the loss of their senior rights". Thus, the words "fair and equitable" include not only the doctrine of strict priority, but also include the principle that senior creditors are entitled to compensation for their entire bundle of rights, and further, that where junior interests participate in a plan, equitable compensation must be made to a creditor for the loss of senior rights.

An application of these principles to the Plan in this proceeding requires a consideration of the rights of the debentureholders and the measure of the compensation they receive for those rights. They have the right to be paid in cash in full at various maturity dates, which range from 1948 to 1966. Until maturity they have the right to receive interest at the rate of 6% per annum, unless prior thereto the debentures are called for payment and in that event, with respect to certain issues, call premiums are also payable. They have in effect security of 2 to 1 for payment of the debentures by operation of the negative pledge covenants.

The Plan provides for payment in full to debentureholders only if we assume that the distribution of the

common stocks of the five operating companies sometime in the future is equivalent to payment in cash.

The Circuit Court found that the bundle was the equitable equivalent of the notes and debentures on the ground that "owning the junior equities is no more speculative than the promise of the corporation whose assets consist of such equities" (R. 213). This is demonstrably unsound. A house which has been appraised at \$5,000 is obviously not the equitable equivalent of a \$5,000 mortgage on two houses that have been appraised at \$5,000 each. The debentureholders have a call on all, not 50%, of the assets of Standard.

Even in equity or bankruptcy reorganization, which presupposes inability to pay debts, the superior rights of a creditor must be recognized by giving additional compensation where he is demoted. *Consolidated Rock Products Co. v. DuBois, supra*. The Commission's opinion (R. 94a-97a) shows that the Commission, while paying lip service to the equitable equivalent and strict priority rules, departs therefrom by depriving the debentureholders of their right to receive both principal and interest in cash and appraises them out of their senior position with common stocks and cash. It gives the debentureholders nothing for their call premiums and refuses to compensate them because of the loss of "senior rights". Surely, creditors of a solvent corporation upon whom a plan is being forced, without vote or representation, under the Act, are entitled to treatment at least equal to that of a creditor of an insolvent corporation being reorganized under Chapter X of the Bankruptcy Act.

### POINT III

**The debentureholders are entitled to their call premium or the equitable equivalent thereof.**

The right of the debentureholders to receive interest to maturity or in the alternative the call premiums (R. 151a-166a), is a contract right of equal dignity with their right to receive the principal of their debentures. The call premium is a device for the benefit of the debtor so that it may, by paying the premium, eliminate its obligation to pay interest to maturity. The Plan (R. 37a) authorized a three year bank loan of \$12,000,000 to bear not more than 3% interest. If this loan were outstanding for a three year period Standard would effect an interest saving of \$1,080,000. The total call premiums on all of the notes and debentures amount to approximately \$995,000. The Plan deprives the debentureholders of this clear right without compensation. As this Court said in *Otis & Co. v. Securities & Exchange Commission, supra* (p. 468):

“Enforcement of an overriding public policy should not have its effect visited upon one class with a corresponding windfall to another class of security holders.”

The debentureholders are entitled to have their contracts performed as written. If, because of the Act, they are not so entitled, they can not be fairly and equitably deprived of this contract right by lip service and without just compensation therefor.

### POINT IV

**If the Act be construed as conferring power upon the Commission arbitrarily to strike down the contract rights of creditors, it is unconstitutional.**

(a)

Valuable property rights of the debentureholders are destroyed without just compensation. These property

rights are taken under Section 11 for the sole purpose of creating theoretically ideal structures in the public utility field deemed to benefit the public generally. The taking of private property for such public purpose has been held by this Court to require a condemnation proceeding with payment of just compensation for the rights taken in order not to violate the due process clause. *Louisville Joint Stock Land Bank v. Radford*, 295 U. S. 555 (1935).

## (b)

There is no lawful process whereby Standard, a solvent corporation, can repudiate a portion of the principal amount of its notes and debentures against the objections of the debentureholders as the plan filed under Section 11 purports to do. Section 11 is not an exercise of the bankruptcy power and cannot be effective as an exercise of that power because of the absence of the jurisdictional fact of insolvency and the lack of essential safeguards such as the requirements of a right to a hearing and the vote of the creditors of a class affected. Creditors' rights can be modified against their objections only by reorganization or liquidation in bankruptcy, and the exercise of the bankruptcy power is dependent upon insolvency in either the bankruptcy or equity sense. *Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pacific Ry. Co.*, 294 U. S. 648 (1935), *Wright v. Union Central Life Insurance Co.*, 304 U. S. 502 (1938). We have found no cases relating to the enforcement of the Sherman Act where the Courts have demoted senior creditors to a stockholder status.

This Court should determine the extent to which the rights of creditors can be affected under Section 11 of the Public Utility Holding Company, and whether or not creditors are entitled to just compensation for the rights so destroyed. The constitutionality of Section 11 of the

Act has not been ruled upon by this Court and *Otis & Co. v. Securities & Exchange Commission, supra*, falls short of determining the question since this Court there held that contract rights were not involved.

The foregoing arguments apply as well to the right of the debentureholders to receive interest to maturity or a call premium as to their right to receive their principal.

### Conclusion

The decision below is a novel departure from doctrines clearly settled by this Court.

The questions are of public concern both from the standpoint of interpretation as well as the administration of the Act and have not been passed upon by this Court. Their determination will affect the investment rights of large numbers of owners of debt securities of public utility holding companies.

For the reasons set forth above, the writs should be granted.

Respectfully submitted,

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